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Project Report

BRITISH COLUMBIA FINANCIAL REVIEW: THE ISSUE OF CROWN AGENCY ACCOUNTABILITY

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Executive Summary—Crown Agency Accountability

This report examines the role of Crown agencies and their relationship with government. The financial health and vitality of these agencies are of central importance to any effort to improve British Columbia's budgetary situation.

The review found clear evidence of insufficient coordination between Crown agencies and the government. In a number of cases examined, Cabinet appeared unaware that it had the capacity to influence the strategic decisions of these agencies.

In at least two other cases Crown agencies were told to pay "dividends" that would have required a bank loan to cover the dividend to be paid in 1991.

We found a profileration of Crown agencies—at least 179 having 16 different types of relationship to the government.

The report recommends that:

- A central coordinating agency with sufficient supervisory powers and resources ensure that Crown agency strategies and business plans support government policy objectives.
- Crown agencies be appropriately accounted for in the Consolidated Revenue Fund to ensure full and accurate financial disclosure.
- A "zero-based" review of all Crown agencies be undertaken to reconfirm their role in the present environment and classify the type of arrangement with government. This may reduce the number of agencies.
- New reporting requirements and standards be developed for government-owned corporations covering corporate objectives, operational and financial information and future-oriented as well as historical information.

The Issue of Crown Agency Accountability

A. Introduction

1. Background

This report considers the creation, mandate, classification, management and accountability of Crown agencies, sometimes referred to as government-owned organizations and enterprises or as Crown corporations.

Crown agencies are established to achieve some aspect of public policy that is judged to be beyond the scope of line ministries. But, regardless of the actual or perceived arm's length relationship between Crown agencies and the government, an effective accountability structure is paramount, such as when the public holds the government accountable for actions or performance by Crown agencies deemed unsatisfactory.

This report examines the types of Crown agencies and their roles and responsibilities in serving public policy objectives. It also considers the appropriateness of the present accountability structure for the wide range of Crown agencies, including finding the balance between the flexibility needed to meet a mandate and a reasonable level of accountability to the government. Finally, we comment on the present process for achieving a coordinated response from the Crown corporations to the public policy objectives of the government and how the present process may be improved. Since the newly established Crown Corporations Secretariat is still substantially in a formative stage, the analysis quite naturally focuses on the present structure. However, we intend this report to assist the new Secretary, Crown Corporations Committee/Executive Council to structure a new and effective mechanism to direct and hold accountable the operations of Crown agencies.

The information in this paper is based on a review of 23 Crown agencies, including all of the 13 major ones, supported by further financial analysis of government-owned enterprises and organizations. In each case, the reporting relationship between the agency and the government was examined to formulate a comprehensive understanding of the existing relationships between Crown agencies and the government.

2. Primary and subsidiary issues

The primary issue surrounding Crown agencies is the lack of an effective government-wide process to ensure that the strategies and performance of the

Crown agencies are supportive of, or consistent with, government public policy objectives. A new balance between the central control framework and an empowered decentralized management process is needed to combine the best features of centralized coordination with decentralized delivery of service delivery.

A subsidiary issue centres on the accountability structure, from the perspective of the management process, the application of accounting principles and reporting. In summary, we recommend changes to the present environment so that:

- A central coordinating agency can ensure that Crown agency strategies and business plans support the government's public policy strategies.
- A central agency has sufficient supervisory powers and resources to monitor the performance of the Crown agencies against approved performance standards.
- Crown agencies, as a direct reflection of their role to serve the public as part of an overall government strategy, are appropriately accounted for in the Consolidated Revenue Fund (CRF) so that the government's primary financial report on the stewardship of public monies is complete and accurate.

There are several subsidiary issues, including:

- The need to perform a "zero-based" review of all Crown agencies, to confirm their present role and placement in the current government environment of policy objectives and more effective resource management.
- The need to define and classify Crown agencies according to appropriate criteria, and to account for them consistently against those criteria.
- The need to clarify reporting and disclosure requirements.
- The need to clarify several related audit and reporting issues.

We have concluded that the nature of the concerns and the potential impact of the options on the Province's overall financial performance and financial position are sufficient to warrant priority action on these issues.

B. Description of Crown agencies

In addition to the activities carried out directly by ministries, the government owns or controls a large number of organizations and enterprises which are instruments of public policy and are mandated to carry out a wide variety of activities. The term "Crown agencies" is widely used within and outside the government to describe these government entities, which include corporations, boards, societies, authorities, councils, commissions and foundations. There appears to be no commonly agreed definition of some of these

entities, including "Crown corporation", a term which has gained widespread but sometimes inaccurate use. Also there is no definitive or officially approved list of Crown corporations. Various incomplete lists exist: invariably B.C. Hydro and Power Authority and B.C. Ferry Corporation appear on such lists but others, such as Workers' Compensation Board and the various Financing Authorities, appear on some lists and not on others.

For their most recent fiscal year, the 41 entities listed in the Summary of Financial Statements of government organizations and enterprises in the 1990/91 Public Accounts had combined assets of $19.8 billion, equity of $2.8 billion, revenues of $9.2 billion and net income of almost $1 billion (see Appendix A) but this excludes numerous other Crown agencies that are not separately disclosed.

An Analysis of the Public Bodies Database, provided to us by the Office of the Comptroller General, is the most recent list of Crown agencies including government-owned corporations. The database identifies 179 public bodies or statutory authorities, excluding the count of multiple groups such as Pension Funds, Hospital and Long-term Care Boards, Cemetery Boards, Libraries, Municipalities, Colleges and Institutes.

Sixteen different arrangements can be seen in the relationships between these bodies and government and in the methods and extent of government control. Twelve of these arrangements apply to fewer than six public bodies each (seven arrangements are conceived for only one or two bodies). The largest single group, 97 in total, includes most of the commissions, councils, societies and committees, which are controlled through their own boards of management.

An analysis of the more substantial public bodies reveals that three groups dominate the financial resources and therefore have the primary accountability requirements. These three groups are as follows:

1. Public bodies that:

    - Are agents of the Crown.
    - Are controlled by government through a government-appointed Board of Directors or Board of Management.
    - Report under the Financial Information Act.

    Seven public bodies are in this category: Provincial Capital Commission, Science Council of B.C., Okanagan Valley Tree Fruit Authority, Glendale Lodge Society, Medical Services Commission, B.C. Housing Management Commission and B.C. Heritage Trust.

2. Public bodies like those above, but which also have their loans guaranteed by government.

    This group contains 13 public bodies: B.C. Trade Development Corporation, B.C. Institute of Technology (BCIT), Colleges and Institutes (several), Expo '86

Corporation (inactive), B.C. Petroleum Corporation, B.C. Educational Institution Capital Financing Authority, B.C. Housing & Employment Development Financing Authority, B.C. Transit Authority, B.C. Building Corporation, B.C. Lottery Corporation, B.C. Systems Corporation, B.C. Hydro and Power Authority, and Insurance Corporation of B.C..

3. Public bodies like those above, but which also have more than 50% of issued voting shares owned by government.

Five public bodies make up this group: B.C. Development Corporation (inactive), B.C. Petroleum (Kitimat) Ltd., B.C. Ferry Corporation, B.C. Steamship Company (1975) Ltd. (inactive), and B.C. Railway Company.

Of the remaining 57 public bodies, 50 are divided into the following arrangements:

Type of Arrangement	Number of Public Bodies
A&C	16
E	9
C&E	5
C,D&E	5
A,B&C	4
D&E	2
B&C	2
A,B,C&E	2
A,C&D	2
B,C,D&E (B.C. Pavilion Corporation)	1
A,B, C & D (B.C. Enterprise Corporation)	1
D (Terry Fox Research Foundation)	1
	50

Arrangement Criteria:

A—Agent of the Crown
B—More than 50 per cent of issued shares are owned by government
C—Controlled by government through a government-appointed Board of Directors or Board of Management
D—Loans are guaranteed by government
E—Report under the Financial Information Act

Three others, B.C. Health Care Systems Society, B.C. International Commercial Arbitration Centre and the International Financial Centre Society of Vancouver, are not classified. Four new numbered corporations have been recently established in Treasury, to direct real estate investments on behalf of pension funds.

This analysis suggests that a proliferation of public bodies has evolved over the years. All of them undoubtedly had a legitimate position in government public policy at the time they were created. They have grown to the point where their number and the variation in

the structural arrangements between them and government, including the extent of government control, is impairing the ability of government to effectively coordinate and plan their roles in the overall strategy. While it was not feasible to study the agencies in any depth, the initial impressions are consistent with the findings in other areas of the overall government review, which has identified significant growth in the number and complexity of government operations and the respective accountability structures.

This analysis illustrates further the diffusion and fragmentation of government agencies, and the challenge to their management and accountability relationship with government. There appear to be ample reasons to carry out a comprehensive review of the role and coordination of public bodies in general and Crown agencies in particular, to reconfirm the need and to seek ways of obtaining a better return on public revenues and expenditures.

The corporate form of organization, usually referred to as Crown corporations, is modelled on conventional practice in Canada and is used extensively by the B.C. government when:

- The Legislative Assembly judges the public interest to be best served by an organization run in accordance with commercial standards. Ministerial control is limited to the definition of general goals and the selection of a competent directing board, leaving the organization free from governmental administrative rules and regulations, such as those relating to personnel and contracts.

- The operations are of a kind requiring a degree of remoteness from the political process. Such an arrangement allows interested and affected parties to be represented on the boards of directors, thereby enhancing public confidence in the impartiality of Crown corporations.

- There is a need to fill gaps in the economy where it would not be reasonable, for financial or national security reasons, to rely on private sector suppliers.

In British Columbia, Crown corporations differ from ministries in that:

- The management and accountability structure usually includes a board of management or directors appointed by the government, at the pleasure of the Lieutenant Governor-in-Council.

- They are not consistently bound by the financial, personnel, contracting, asset disposal and general administrative rules applicable to government ministries.

- They are generally subject to a far less rigorous regime of direction, control and accountability than that to which ministries must conform.

- They have separate legal identities and are considered distinct from the government and the related ministry.

- Investments in and loans to Crown corporations are considered to be assets of the government in the CRF: similar transactions within government

departments are charged to current expenditures and included in the annual deficit.

These characteristics should be considered in the formulation of a new and more responsive process to coordinate Crown corporation strategies with public policy and install the associated accountability structure.

C. Analysis of B.C. government corporations

1. Government-owned organizations reported in the Public Accounts

The 1990/91 Public Accounts lists 41 separate provincial government organizations and enterprises and contains the annual financial statements for each. All but three are audited, one of the three being a small inactive company.

The organizations conduct a wide range of activities using different operating characteristics. Included are small societies and authorities carrying out government-type activities requiring 100% government funding, and large operating Crown corporations such as B.C. Hydro and B.C. Rail which have virtually autonomous business missions and independent revenue streams. Appendix A sets out summary financial information for the most significant of the 41 organizations listed in the Public Accounts and totals for the rest.

A review of this information reveals the following:

- Four of the entities, the Medical Service Commission of B.C. and the three Financing Authorities, are funding conduits which pass through government contributions or borrowings to finance public programs and activities that could be carried out directly by the government.

- Twenty-four of the 41 entities, in aggregate, represent only $226 million in assets, $232 million in revenues and $12 million in annual net earnings. All of these entities depend on government appropriations or on interest generated from previous government contributions for all or a substantial portion of their revenue. Many also receive administrative services without charge from the government. None of them are commercially viable and most appear to fulfill a specific phase of a government program. For example, the B.C. Heritage Trust, which is designated a Crown corporation by its Act, receives virtually all of its revenue from provincial government grants and from interest on capital contributed by the province. The stated purpose of this corporation is to encourage and facilitate the protection and conservation of heritage property in the province.

- At March 31, 1991, the remaining 13 corporations represented assets of $16.9 billion, equity of $2.7 billion and revenues and net profit of $7.3 billion and $945 million respectively. These are the principal entities

which are commonly referred to as Crown corporations. Two other significant government-controlled entities, Workers' Compensation Board and Credit Union Deposit Insurance Corporation, are excluded from the listing of corporations in Volume 2 of the 1990/91 Public Accounts, but their audited financial statements are published in the Public Accounts.

2. Characteristics of Crown corporations

The 13 entities clearly identified as Crown corporations can be profiled as follows:

- The B.C. Hydro and Power Authority is the largest Crown corporation and at March 31, 1991, represented assets of $9.3 billion, equity of $762 million, sales of $1.9 billion and net income of $207 million. It holds a virtual monopoly position for the generation and distribution of electricity in B.C., but competes with other minor sources of power. Although it has debt owing to or guaranteed by the province totalling $7.1 billion, the corporation is generally considered to be commercial in nature and financially viable.

- ICBC provides automobile insurance on a monopoly basis in B.C. Its revenues now exceed $1.8 billion and it manages investments in excess of $2.7 billion. It is self-sustaining and has received no operating or capital funds from the province with one exception: on March 31, 1976, the provincial government authorized a grant of $181.5 million to the Corporation. It is also considered to be commercial in nature and financially viable.

- The three major transportation Crown corporations, British Columbia Transit ("B.C. Transit"), British Columbia Railway Company ("B.C. Rail") and British Columbia Ferry Corporation ("B.C. Ferry") are all important elements of the government's transportation policy. All have significant loans from or guarantees by the province and significant capital contributed by the province. Current year appropriations to B.C. Transit exceed $200 million whereas appropriations to B.C. Rail and B.C. Ferry were much smaller. Appropriations to B.C. Rail were specifically attributed to uneconomic services deemed to be in the public interest. It appears that all three companies are in a competitive situation, but there is a range of financial dependence on the Province.

- Two corporations, British Columbia Buildings Corporation and British Columbia Systems Corporation ("BCSC"), were established to provide services to the government—office space and information technology—from new corporate structures that could apply a full costing approach to the services provided. A number of other governments obtain these services from within and do not establish separate corporations. While some limited services are provided to the private sector (BCSC is prohibited from doing so) and with over 90% of revenues coming from the provincial government, both are clearly dependent on government for service requirements and revenue.

- B.C. Pavilion Corp. and Pacific National Exhibition operate public facilities which compete for revenues with the private sector. However, B.C. Pavilion depends on government for funding; it has a contributed surplus from the government of $155 million, has no debt, and receives annual contributions for operations from the province.

- Provincial Rental Housing Corporation operates subsidized housing units and depends on significant government contributions to support low rental housing. British Columbia Petroleum Corporation transferred its marketing operations to the private sector in 1990. It is now primarily an administrative and regulatory body which determines royalty payments and industry levies, and provides information to assist the government with policy decisions. Both corporations are clearly engaged in government-type activities.

Other branches of ministries and corporations provide services to the public on a virtual monopoly basis. Agencies of this type generate significant net revenues for the Province which constitute a clear form of taxation. Examples are the Liquor Distribution Branch (LDB) and B.C. Lottery Corporation. The LDB is a branch of the Ministry of the Attorney General, but in its mandate and operating characteristics is much closer to a self-sufficient Crown corporation than a governmental agency.

3. Classification of government-owned organizations

The preceding analysis demonstrates that government-owned entities have a wide range of characteristics. At one end of the spectrum, the entities receive full funding from the government and carry out activities which are fundamentally governmental in nature and unlikely to be undertaken by the private sector. While a corporate structure may be appropriate for operational reasons, such non-financial considerations should not override the need for controls which recognize the true nature of the entity and the source of its funds.

At the other extreme, the entities are commercial in nature and not dependent on government funding. In some cases, such funding is virtually prohibited by the legislative mandate. The range in mandate should be matched by accountability regimes that recognize the governmental or commercial nature of the service and whether revenues are from the government or directly from consumers. The accountability regimes for such corporations should also consider that ownership and the source of back-up financial resources, in the circumstance of an operational or financial crisis, is ultimately the government. Such was the case for ICBC in 1976.

At present, there is no classification of Crown corporations into logical sets based on criteria such as type of mandate, source of funding, corporate structure and the degree of direction, control and accountability exercised by government. The existing classification plan is mainly for accounting purpose. As described in a previous section, the most recent government public bodies data base provided by the Office of the Comptroller General identifies more than 179 public bodies, and

classifies their relationship with government within the 18 responsible ministries using the following criteria:

- An agent of the Crown under an enactment.
- A public body that issues voting shares: the government owns more than 50% of the shares that have been issued.
- A public body controlled by government: a majority of the members of the public body or of its board of directors or board of management consists of either or both of persons appointed as members by the Lieutenant Governor-in-Council, by a Minister or by an Act, or public officers acting as such.
- A public body whose borrowings are guaranteed by the Crown.
- A public body required to report under the Financial Information Act.

In many respects, all government corporations have a homogeneous and very limited set of formal rules with which they must comply, as well as some degree of operational independence and freedom from the tighter controls applied to ministries. This may be appropriate for corporations which compete in a private sector model and are self-sustaining, but is much less so for the many government corporations carrying out government-type activities and heavily dependent on government appropriations for their financing. In view of the extreme range of the characteristics of government-owned enterprises, it seems inconsistent to continue subjecting all of them to what is essentially a uniform and quite limited set of government controls.

4. Financing of government-owned corporations

Government-owned corporations are financed by three main sources:

- Equity investment comprised of:
  - Share capital.
  - Capital contributed in the form of fixed assets, such as ferries, railway assets and land.
  - Accumulated earnings—the excess of earnings of the corporation over amounts paid to government through dividends.
- Loans from government—interest-bearing with specified terms of repayment.
- Non-government loans—interest-bearing with specified terms of repayment, and fully guaranteed by the government.

Equity financing

In the private sector, equity financing represents the shareholders' equity in a company and provides an important point of reference for the lenders who typically provide the rest of the required capital. Shareholders expect a reasonable rate of return on their equity and measure the performance of management, in part, by how the percentage return compares to other potential investment and risk opportunities.

Such measures are not meaningful for government-owned corporations which depend on government funding. For these corporations, equity represents a form of free capital which obscures the commercial cost of their activities and therefore their financial accountability. For example, Pacific National Exhibition at March 31, 1991, had equity of $30 million and net income of $0.9 million. If it were operated on a commercial basis instead of as part of a government program, and interest were computed on the corporation's equity at 9 1/2%, the current government long-term borrowing rate, the corporation would have incurred a loss of $2.0 million. On this basis, a government appropriation would be required to fund the current deficit and the activities and financial performance of the corporation would be subjected to increased scrutiny.

The use of retained earnings to finance current losses has the same effect, in that no reviews or approvals are required, even though government funds are expended. We recommend that the use of equity funding for governmental, dependent corporations be eliminated where practical so that all the costs associated with program delivery are properly recognized.

Debt financing

We have noted instances where government-sourced debt financing has been used when the government corporation involved was unable to meet required interest and principal payments. An example is B.C. Transit which has long-term debt in excess of $1.2 billion and required operating contributions from the province in excess of $200 million. In accordance with an agreement with B.C. Transit, future government funding of all principal and interest payments on $275 million of the corporation's long-term debt was arranged in 1986.

If the intention of such advances to commercially-styled corporations is to recover the related costs from end users, the funds should be advanced in the form of a loan. If the intention is to subsidize an operation, a contribution should be clearly disclosed in the accounts of the corporation and the government. Advances which have the effect of a contribution but take the form of a loan are inappropriate: they distort the financial position and the accountability of the corporation to the government under the current accounting policies, including overstating the government's assets and understating the deficit.

We recommend that the method of financing a government corporation correspond to the true nature of the transaction, the intended financial effect

on the corporation's financial performance and the expected outcome of the investment, based on an approved business case to support the transaction.

Fiscal agency agreements

Fiscal agency agreements were adopted as a result of the introduction of the new Financial Administration Act (FAA) in 1981. A principal purpose of the FAA was to improve accountability and control over government finances and the financial activities of government agencies. The FAA allows for the appointment of the Minister of Finance and Corporate Relations as Fiscal Agent for the government and its agencies. Several Crown corporation statutes designate the minister as Fiscal Agent for the purposes of those Crown corporations.

As part of this initiative, the Provincial Treasury division of the Ministry of Finance and Corporate Relations was established to centralize treasury functions and to provide efficient financial services and where appropriate control over government corporations. Fiscal agency agreements were in turn concluded to outline the sharing of responsibilities between Crown corporations and the Province in various financial areas.

The agreements, many of which have been in place since the early 1980s, cover such areas as debt issuance, investment activities, rating agency relations, investment banker relations, loans and guarantees, derivative products and financial reporting.

In most cases, the bulk of these activities are performed centrally in the Provincial Treasury Division of the Ministry, on behalf of (and in consultation with) the Crown corporations. The arrangement works well and generally provides the coordination necessary to ensure an integrated approach to financial markets.

The framework of fiscal agency agreements is virtually complete. All Crown corporations, with the exception of the Insurance Corporation of British Columbia (ICBC) which manages a significant investment portfolio, have such agreements with the Province. We recommend that a fiscal agency agreement be concluded between ICBC and the Province.

D. Implications of the corporate structure on accountability

For many government corporations, the nature of their operations closely parallels the activities of ministries and they depend on government financial support for their existence. Others are quite similar to the private sector in terms of their activities and financial viability. Notwithstanding this difference, the corporate structure appears to result in all provincial government corporations being treated as a relatively homogeneous group, exempt from most of the management processes, reviews, rules and reporting requirements applicable to ministries.

The information now required of government-owned corporations is minimal and after the fact. Even for the most commercial and financially independent, the structure does not represent an appropriate framework for government to effectively influence strategic choices or for the Legislative Assembly to hold them ultimately accountable. The major components of the present framework are:

- The Financial Administration Act, which is the principal source of provincial government financial legislation. It generally does not apply to government corporations or other public bodies, but it contains several provisions that permit the Comptroller General to have access to Crown corporation information if required.

- The Financial Information Act, which requires only certain routine historical financial information to be prepared and made available by corporations. Schedule 2 of the Act, which identifies corporations subject to the Act, appears to require amendment because it contains a number of entities which no longer exist.

- The enabling Acts that establish many corporations generally require reporting similar to that required under the FIA, including a requirement to table the financial statements and an annual report in the Legislative Assembly. But, the information produced is quite limited. However, the Public Accounts Committee can require Crown corporations to appear before it.

- The appointment of a board of directors or board of management, which usually includes the Minister responsible for the corporation.

- The submission required for the Estimates, which contain no information on corporate plans and have inadequate support for current appropriations. Other deficiencies include the following:

  - Current appropriations are generally made by way of grants, and no supporting information is given.

  - There is no separate display or approval of loans from the government to corporations.

  - There is no display at all of proposed loans by corporations from outside sources.

  - There is no review of funding for many corporations since all funding comes from their own revenues (e.g., B.C. Lottery).

- Annual Reports published by many corporations, some of which are similar in appearance and content to those prepared by public companies. However, there are no rules as to disclosure required and few reports contain information about the achievement of corporate goals or future directions, strategies and plans.

In addition to providing information to the Legislative Assembly, each corporation is responsible to a Minister and may also have a relationship with central agencies of government. Ministers responsible for government-owned corporations typically sit on the corporations' boards of directors. This facilitates the communication of government priorities on public policy matters and initiatives and provides for a supervisory role by the ministers. We understand that in practice there is a wide variation in the type and extent of communication between ministries and the corporations for which they are responsible, which understandably reflects the personal styles of the officials involved and the degree of control exercised by the ministry.

Our discussions with program analysts in Treasury Board staff indicated there is no statutory requirement for corporations to provide information to Treasury Board concerning their plans, with the result that different levels of monitoring and review and approval of plans are applied to government corporations. Even when ongoing government financial support is required, sometimes up to 100% of their needs, corporations usually receive it in the form of grants from their responsible ministries, and the relevant supporting information provided to Treasury Board may be no more extensive than for any other grant by government. While there appears to be more Treasury Board involvement with certain corporations requiring financial support or which provide government services, such as B.C. Buildings Corporation, it is clear that, in many cases, scrutiny and monitoring of government-owned corporations by central agencies is very limited and concerned primarily with retrospective demonstrations of formal compliance.

However, there is a second more significant matter than after-the-fact accountability: that is the government's capacity to know of and influence the major strategic choices that can affect both the financial future of the agency and public service cost and quality. There is evidence that government-owned corporations have engaged in major activities that government is not aware of, leading to non-compliance with overall government strategy. Also, there are examples of duplication of services and support infrastructures and the attendant costs and overlap. Central coordination of all the agencies of government to deliver the government's overall program requires direct involvement in the planning, design and delivery of the individual programs, as well as accountability for the results.

In his 1990 report, the Auditor General addressed accountability issues concerning the major Crown corporations. He recommended improvements in reporting to ensure that the Legislative Assembly would be informed of corporate objectives, progress in achieving those objectives and the discharge of mandates with due regard for economy and efficiency.

The Auditor General recommended that a framework for accountability be designed for the major Crown corporations to cover operational and financial information, and future-oriented as well as historical information. In designing the framework for accountability reporting, the Auditor General also recommended that the government consider adopting the approach to effectiveness reporting proposed by the Canadian Comprehensive Auditing Foundation.

We strongly support the Auditor General's conclusions and recommendations and urge the government to proceed with changes to establish the required framework.

E. Issues

1. Central review and coordination of operational and financial plans

At present, there is no requirement for government-owned corporations to present information on their future plans to the Legislative Assembly. Furthermore, program analysts in Treasury Board confirmed there is no requirement to provide future-oriented information to central agencies of government. However, the 1990 Annual Report of the Auditor General commented favourably on the information provided by several corporations, including B.C. Hydro and B.C. Pavilion Corporation, emphasizing the quality of information on their objectives and performance targets. Therefore, while some responsible ministries and Treasury Board analysts request and receive information on future plans of corporations, this is an informal process with no apparent structure or consistency. Since there is no appropriate process for the review and approval of corporate plans, accountability for achievement of plans is also seriously diminished.

We believe that corporations which are governmental in nature or depend on government funding should provide a corporate plan similar to that required of federal Crown corporations and private sector business. Elements of the corporate plan which would cover a 4 to 5 year time frame would include:

- Mandate.
- Corporate objectives and strategies.
- Major initiatives.
- Outputs (quantitative and qualitative including cost per unit, where applicable).
- Performance targets.
- Financial requirements and sources.
- New thrusts.
- Detailed annual operating budget for budget year and summary information for succeeding two years.
- Detailed capital budget for budget year and summary estimated capital commitments for succeeding two years.

The corporate plan should require approval by the corporation's Board of Directors, the responsible ministry, and by Treasury Board or other central agency. The Legislative Assembly would receive summary information in the Estimates and the full corporate plan would be tabled in the Legislature. The summary information in the Estimates would provide support for current appropriations and would also serve as a basis for establishing accountability for the results of each corporation.

This information would also be aggregated with information for the responsible ministry so that central agencies and the Legislative Assembly would be able to examine the full program of a ministry, whether carried out in governmental or corporate form.

To assist corporations in responding to the government's need for information on these plans, Treasury Board or some other appropriate body should set out the overall requirements for a corporate plan. Specific information requirements for individual corporations should be agreed on between a central agency, the responsible ministry and the corporation and documented and updated on an annual basis.

For corporations which are commercial in nature and do not depend on government funding, similar requirements for a corporate plan should be established, based on the framework already in existence. While such information may be quite different than for governmental, dependent corporations, all Crown corporations are instruments of public policy. Therefore, it is important to establish a coordinated planning and reporting process that integrates this information and displays how the corporation's plans fit into overall governmental and ministry policies and programs.

The need for a mechanism that ensures effective communication between Crown agencies, the Minister responsible and a central agency responsible for ensuring that the strategic directions of the Crowns are consistent with overall government policy is illustrated further by several significant breakdowns in the communications process.

One such incident involves B.C. Buildings Corporation and the Oakalla project. In this instance, BCBC has undertaken a comprehensive planning process and rezoning of the former Oakalla properties comprising some 67 acres to be developed and sold in an open market. The planning process undertaken by BCBC and its consultants was in the view of the corporation fully disclosed to the corporation's Minister responsible and Board of Directors, including gaining their approval of various key decisions throughout the process. The corporation contends that the Minister was kept fully apprised of developments. Hence, there was no need, in its view, to take any further steps with respect to briefing others in government including Treasury Board, on the assumption that the Minister responsible was properly advising the Cabinet and other central agencies.

In this example, Treasury Board staff has stated very clearly that they were not involved in the key planning decisions on this property and were not aware of BCBC plans and resultant commitments. BCBC is equally adamant that it has followed due process through its Minister and Board of Directors and that all key decisions were approved along the way. The issue is not whether the corporation acted properly in planning for the former Oakalla lands but whether there is an effective process for communicating major decisions and initiatives being taken by Crown agencies to an appropriate coordinating body in government.

The reasons the communication did not reach the appropriate persons and elicit the requested response are not clear, but it shows the need for a central agency to have

the mandate to manage the overall relationship and communication between Crown agencies and the government on strategic and major issues. Government must be kept informed of all major plans and activities that are covered by annual business plans as well as major developments within those business plans as they occur. This suggests that a central agency to coordinate the planning, approval and developmental stages of any major Crown agencies initiatives is a prerequisite condition for the effective coordination of Crown activity.

2. The need for classification and reconfirmation of government-owned corporations

Government corporations have been allowed a control and accountability framework significantly different from that to which government ministries are subjected. This difference is manifested in:

- The lack of review and challenge of corporation plans by government agencies or elected representatives.
- The freedom corporations have from financial, personnel, asset disposal and general administration rules which are applicable to ministries.
- The arm's-length accounting rules applied to corporations by the government.
- The general attitude of independence that seems to exist within government-owned corporations.

This relief from ministerial accountability and control appears to have evolved because their mandate and operating approach have been considered similar to those of privately owned organizations. However, the characteristics of most of the provincial corporations are actually very similar to those of ministries: they are dependent on government appropriations and carry out activities which are unlikely to be undertaken by the private sector. For these corporations, we believe that the difference in their accountability regimes from the framework applicable to ministries is too pronounced and that significant changes are necessary.

The commercial and self-sustaining nature of other operations, however, justifies controls which are less rigorous than those applicable to ministries and to dependent non-commercial corporations. For these corporations, the public interest can be protected, in part, by adapting a true corporate structure and operating process and by comparing performance to similar organizations in the private sector.

Government-owned corporations should be classified according to their dependence on government appropriations and the nature of their operations. For those which carry out governmental activities or are dependent on government funds, an accountability regime closer to that applied to ministries needs to be constructed and instituted. Conversely, a framework is needed for corporations of a commercial, self-sufficient nature that recognizes a greater need for operational independence from government within a framework of an agreed public policy role

and responsibility. Also, government corporations should be classified according to the degree of management direction and financial control the government desires.

Criteria could be established to segregate these corporations into logical groups and an appropriate accountability framework and reporting structure should be designed for each classification. The newly "scheduled" Crown corporations could be appended to the Financial Administration Act with significant amendments, or to a new Act. Regular reviews of the classifications and the scheduling of individual corporations should be carried out by a central agency to address changes in corporation operations and the accountability structure.

The proliferation of Crown agencies with widely different mandates and roles suggests that many may be difficult to classify. In some cases, the original need may have changed or been overtaken by events, new priorities or better solutions. A critical review of all public bodies and Crown agencies to reconfirm their role in government should be completed in conjunction with the classification process. This review should adopt a zero-based approach that reexamines the need for each Crown agency against criteria focussing on mission, public policy role, costs and measurable benefits to put a disciplined structure around the review process.

3. Accounting for government corporate investments

Current practice

In the Public Accounts government organizations are distinguished from the government corporations described as enterprises. The major entities listed as "enterprises" are generally Crown corporations and are commercial in style and mandate. Other enterprises and "organizations" are more governmental in nature. While the distinction between the two groups may be obscure, it yields different accounting treatments for the government's investments in these two types of corporations in the Public Accounts. The accounting policies followed for these corporate investments in the CRF and the Summary Financial Statements are shown in the table below.

	Consolidated Revenue Fund Financial Statements	Summary Financial Statements
(1) Investment carrying value:		
- Government enterprises	At original cost, or less if value impaired.	At modified equity, which includes original cost plus earnings/losses and other net equity changes of the enterprises, using the enterprises accounting policies rather than the government's
- Government organizations (other than government enterprises)	At original cost, or less if value impaired.	Consolidated on a line-by-line basis after adjusting to government accounting policies.
(2) Recognition of revenue/ expenditure		
- Government enterprises	Dividends paid to government recorded as revenue.	Earnings/losses included in revenue
- Government organizations (other than government enterprises)	Dividends paid to government recorded as revenue.	Consolidated on a line-by-line basis after adjusting to government accounting policies.

In conformity with the proposed accounting policies arising from the overall financial review, we believe that the CRF financial statements are the principal financial statements of the government. This view is also consistent with the position taken by the Auditor General for many years. It is important, therefore, that they present fairly the government's investments in corporations.

The result of the current accounting policies is that the CRF financial statements present a much less complete picture of the government's corporate investments than presented by the Summary Financial Statements, which reflect the governmental nature of "organizations" and consolidate their accounts after converting them to government accounting policies. For government enterprises, the Summary Financial Statements include all of the earnings (or losses) reported in the enterprise's financial statements instead of the dividends paid to government. However, the CRF financial statements reflect dividends received from the enterprises only, and thus do not recognize earnings which have accumulated within a corporation. This results in a significant difference between the carrying value of corporate investments in the CRF financial statements and the amount of equity shown in the financial statements of the corporation.

The most graphic example of this is the B.C. Hydro and Power Authority which, at March 31, 1991, had $747 million in retained earnings which, under current accounting policies, is not recognized in the CRF until it is ultimately declared as a dividend to the province. Under the rules of the present dividend agreement with B.C. Hydro, retained earnings are building up at the rate of approximately $50 million per year. As a direct consequence of this

accounting policy, the CRF financial statements at March 31, 1991, overstated the accumulated deficit of the province by $747 million and overstated the current year's deficit by $62 million after a dividend payment of $145 million, with respect to the accounting for B.C. Hydro alone.

We have not attempted to quantify the effect for the other Crown agencies, as the decisions concerning the classification of these agencies and the recommended accounting policy to be applied to them have not been made. However, in the years that we reviewed, dividends paid to the government were consistently lower than corporate earnings and the government deficit was overstated by that difference. For example, the government could require B.C. Hydro to pay out all of its retained earnings from prior years, as a dividend, but under the existing accounting policy this would be applied to reduce the current year's deficit reported in the CRF financial statements. Such treatment would produce a major distortion in the current year's financial results of the provincial government. Nevertheless, under the present accounting policies the accumulated deficit is overstated by that amount. Furthermore, any such payment made in these circumstances could of course result in a corresponding increase in debt, in this case by B.C. Hydro, but also by any other dividend-paying Crown agency.

During our review, we encountered an example of "window-dressing" that the present accounting policy makes possible. During the current fiscal year, BCBC was directed by Treasury Board to issue a $25.0 million dividend to the government. A dividend of about $11.0 million would have allowed the corporation to maintain its targeted debt/equity ratio at the end of the year and thus would normally have been declared. Further, in the current fiscal year, Treasury Board directed BCBC to absorb a portion of its normal price increases to result in a saving to client ministries of about $7.5 million. Accounting for wholly owned corporations such as BCBC which are governmental in nature by consolidating them in the CRF, as is done in the Summary Financial Statements, would neutralize the effect of such tactics and therefore eliminate them.

The present accounting policies for the CRF provide other challenges that could cause government to focus unduly on dividend recovery from government corporations and not be as concerned with major business issues which may not directly or immediately affect dividends but have a profound long-term impact on the financial and operational health of the corporation. The present accounting treatment of B.C. Rail interests in the North East Coal Line and the associated Quintette Coal reorganization is an example. There is a possibility of a future write-down of B.C. Rail interests linked to the ultimate outcome of the Quintette reorganization. If such a write-down were to occur, even if it were very material it might have no direct effect on the government's accounts, because the CRF carrying value for B.C. Rail is about $650 million less than the shareholders' equity in the company. Such an outcome at least highlights the inconsistency and ambiguity that exists in the accounting for the government's corporate investments. The proposed accounting treatment would eliminate such ambiguities and cause government as the public shareholder to focus on all of the activities of its corporations.

Recommended practice

Our companion report on accounting policies recommends that the accounting policies for the government's corporate investments now applied in the Summary Financial Statements should become the government standard, and that only one set of financial statements be prepared, thus eliminating the differences between the CRF and Summary Financial Statements. In effect, the new CRF would cover the broad entity of government, including the Crown corporations.

If this policy is adopted, it is important that corporations be classified properly, distinguishing those which are consolidated after conversion to government accounting principles from those which are accounted for on the modified equity basis using their own accounting principles. The difference between these two policies is significant. For example, the fixed assets of a corporation which is consolidated are written off as are fixed assets purchased directly by government, whereas fixed assets of corporations accounted for on a modified equity basis are included in the government's equity at net book value.

The government's accounting for its investment in B.C. Pavilion Corporation illustrates the significance of accounting policies applied to specific corporations. It also provides an example of a corporation now accounted for on the modified equity basis in the Summary Financial Statements, whose characteristics indicate that full consolidation would now be appropriate. B.C. Pavilion Corp. discloses equity in its financial statements of $152 million which approximates its carrying value in the CRF and consists almost entirely of its investment in B.C. Place Stadium. Even though this asset is financed entirely by equity, the corporation posted in its March 31, 1991 financial statements a loss of $2 million after receiving an operating subsidy of $3 million from the government. Because of the significant contributed capital and the ongoing financial support it requires, it is clear that this corporation is financially dependent on the government.

Our recommendations on accounting policies would require its accounts to be consolidated in the CRF financial statements after adjusting to government accounting policies. Government accounting policy, which writes off fixed assets at the time of purchase, would eliminate all of the fixed assets and the equity of B.C. Pavilion Corporation, now carried as an asset in both the CRF and the Summary Financial Statements. The principle of this accounting treatment appears consistent with government accounting policy, since the fixed assets of B.C. Pavilion Corporation, principally B.C. Place Stadium, are similar to other government fixed assets which do not generate a direct financial return but could create substantial secondary benefits.

Corporations accounted for using the modified equity method should be those self-sufficient corporations whose activities are not governmental in nature and therefore whose accounts should not be consolidated with the other activities of government. This is consistent with the basic concept of

segregating governmental from commercial activities undertaken under the auspices of the government.

4. Annual reports

Most government corporations prepare Annual Reports. The formats vary significantly; some Annual Reports are glossy publications that in format, content and cost are very similar to those prepared by public companies, which use their annual reports as a means to sell themselves to the public. Other corporations produce Annual Reports with restricted information, such as the financial statements required under the Financial Information Act or their own Act. We noted that Annual Reports produced by corporations normally do not disclose information on plans and objectives, on outputs and related unit costs, and financial results compared to budgets. At the moment, tabling of the Annual Reports in the Legislative Assembly is one of the few accountability processes in place, and it is post facto and somewhat perfunctory.

It is important that Annual Reports be prepared to serve as an accountability mechanism and that they report on actual results achieved in relation to objectives set out in the corporate plan. Therefore, guidance should be developed by the central agency, the responsible ministry and the corporation on the standards and contents of Annual Reports of government-owned corporations, including agreement on the specific minimum information required from individual corporations.

5. Independent audit

Two government corporations and one significant branch do not have an audit opinion expressed on their financial statements. One of these, 178561 B.C. Ltd. (formerly Pacific Coach Lines Limited), is inactive. The other two are the LDB and Okanagan Valley Tree Fruit Authority.

The LDB has annual sales in excess of $1.3 billion and net income in excess of $400 million. It maintains its own accounting system based upon generally accepted accounting principles, is generally subject to the controls required by the Financial Administration Act but is not subject to specific Treasury Board directives. While the Auditor General performs work on the LDB accounts in the context of his opinion on the overall provincial financial statements, no separate audit opinion is given on the LDB financial statements. In view of the unique status of the LDB in government, the control issues inherent in the liquor distribution business, and the dollar amounts involved, we believe its financial statements should receive a separate audit.

The Okanagan Valley Tree Fruit Authority is funded entirely by the province and we believe that its accounts should also be subjected to an independent audit.

The Auditor General Act provides for the Auditor General to carry out value-for-money audits within the government and in the corporations that are audited by the office. Private sector firms audit a number of government corporations and some of

them belong in the governmental service classification which depends heavily on government funding.

We recommend that all government corporations should be subject to the same standards regardless of audit appointment. Accordingly, legislation should be established to provide for independent special examinations, or value-for-money audits, to be performed on all government agencies.

6. Intervention in Crown management

Instances of political involvement in day-to-day operational matters, which should be the responsibility of corporate management, have been identified. Examples include a request to B.C. Building Corporation to reduce space charges to government entities by $7.5 million in 1991/92, a direction to B.C. Transit to increase the number of stations on the SkyTrain extension to Whalley and the reduction of preventive maintenance at B.C. Hydro in the mid 1980s to lower levels that have created a significant maintenance deficit that will be recovered over the next five years or so. While there is no mechanism that could ever prevent the occurrence of this type of intervention, the existence of formal and approved business plans which are tabled with the appropriate central agency and available for public scrutiny can make inappropriate interventions at the operating level more evident and thus less likely.

F. Planning, direction and control

Existing planning, direction, control and monitoring practices of a government-owned corporation originate from a number of sources including the Board of Directors, the responsible Minister and Ministry staff, Treasury Board and its staff, and where loans are required, the Minister of Finance and Corporate Relations. Notwithstanding the number of involved parties, it appears that some fundamentally critical elements of an appropriate planning and accountability framework are not in place to plan and coordinate their behavior.

Many of the government's corporations are carrying out operations similar to those of ministries, using funding from the same source, but there are also several significant, autonomous business operations. At present, the Office of the Comptroller General is responsible for providing a financial management infrastructure for ministries, including detailed standards, procedures and policies, and training of financial personnel, but the corporations receive no such leadership and assistance.

Earlier in this chapter, we recommended that a central agency take responsibility for:

- Classifying government-owned corporations under expanded or new legislation addressing government-owned corporations, including regular reviews to make any necessary reclassifications.

- Setting out overall requirements for a corporate plan and agreeing on specific information requirements for individual corporations.

- Reviewing and challenging corporate plans including agreeing on corporate objectives and strategies, performance targets, and performance measurement factors.

- Providing guidance on the contents of annual reports of government-owned corporations and agreeing on the specific minimum information to be provided by individual corporations.

Commercial, self-sustaining corporations are generally structured more like companies in the private sector and in many cases, have internal resources that reduce the need for proactive financial management leadership from a central agency. Nevertheless, many corporations within private sector conglomerates receive guidance and monitoring similar to that recommended above, from a holding company or a head office. The specific role of a central agency in the financial planning and management area with respect to the few commercial, self-sustaining corporations in government should be developed and tailored to the specific circumstances for each corporation. However, the arrangements should support the principles of the management and control framework established by the central planning and management agency of government responsible for coordinating Crown corporations with overall government fiscal plans and management processes.

In the case of government-owned corporations, central agencies responsibility should be expanded to include:

- Setting government-wide standards and guidelines in the financial planning and management area and interacting with corporations as necessary.

- Approving and monitoring budgetary control, financial reporting and control systems.

- Monitoring ongoing results in relation to the approved business plan.

- Assisting with the training of financial staff and where appropriate, assisting with the selection and development of financial staff.

- Establishing standards for internal audit and monitoring internal audit activity.

We see a role for a new and distinctly qualified central agency such as the Crown Corporations Secretariat to provide leadership in the crucial area of strategic and financial planning and management, and to maintain the context and a balance between the corporations' missions and their contribution to public policy.

The principles of such a relationship should consider and could include:

- The appointment of experienced and professional Boards of Directors.

- The engagement of seasoned chief executives and management teams.

- The appointment of a member of the Crown Corporations Secretariat as an ex-officio member of each Board of Directors.

- A review and challenge process that focuses on the corporate strategy and specific plans of the corporation to ensure consistency with overall government direction and with its own mission.

- Monitoring and approving the business plans and major corporate initiatives.

- Monitoring budgetary and operating performance against plan and performance standards.

- Ensuring that the public perception of the corporation corresponds with the image defined by overall government policy, and that situations are avoided that could inadvertently place the Minister responsible or government in an unfavourable position.

The guiding principle in this relationship could be described as flexibility: ideally the empowered Board of Directors and management discharge their responsibilities to the government with little direct intervention from the central agency once the overall strategy and plan has been accepted. Conversely, the central agency would need to take a more proactive role in the direction and management of the corporation, an undesirable but necessary consequence, if Crown agency performance is unsatisfactory.

APPENDIX A

GOVERNMENT-OWNED ORGANIZATIONS AND ENTERPRISES

AS LISTED IN THE 1990/91 PUBLIC ACCOUNTS

($millions)

	Per Corporations Financial Statements (A)									(F)
	Assets	Total Liabilities	Net Debt (B)	Equity	Total Revenue	Expenses	Net Profit	Appropriation Purpose	Amount	Investments in & amounts due
Transportation										
British Columbia Ferry Corporation	$442	279	60	163	260	264	(4)(C)	Operating subsidy	13	$-
								Capital subsidy	35	
								Free use of ships	5	-
British Columbia Railway Company	1,330	388	287	942	299	266	33(D)	Specific subsidies	13	268
								Property & equipment	3	-
British Columbia Transit	1,630	1,424	1,228	206	466	464	2	Operating subsidy	173	-
								Debt servicing	40	-
Government and Other										
British Columbia Buildings Corporation	736	610	514	126	298	278	20		-	24
British Columbia Hydro & Power Authority	9,257	8,495	7,152	762	1,909	1,702	207		-	122
British Columbia Liquor Distribution Branch	60	60	-	-	1,334	889	445		-	-
British Columbia Lottery Corporation	70	70	-	-	603	386	217		-	15
British Columbia Pavilion Corporation	157	5	-	152	31	33	(2)	Operations	3	154
								Fixed assets	1	
B.C. Petroleum Corporation	7	6	-	1	113	116	(3)		-	-
British Columbia Systems Corporation	76	57	34	19	155	145	10		-	-
I.C.B.C.	2,887	2,719	-	168	1,745	1,728	17		-	-
Provincial Rental Housing Corporation	200	80	-	120	9	7	2	Operating subsidy	30	21
Pacific National Exhibition	34	3	-	31	28	27	1		-	-
	16,886	14,196	9,275	2,690	7,250	6,305	945		316	604
Financing Authorities										
School Districts, Regional Hospital Districts and Educational Institutions	2,470	2,470	2,350	-	383	383	-		-	15
Medical Services Commission of B.C.	239	239	-	-	1,351	1,351	-		1,351	-
	19,595	16,905	11,625	2,690	8,984	8,039	945		1,667	619
Remaining 24 Entities	226	147	851	79	232	220	12		(E)	-
	$19,821	17,052	12,476	2,769	9,216	8,259	957			$619

NOTES:

The data have been rounded and may contain minor differences.

(A) For corporations the latest fiscal year is 12 months ended December 30, 1990 or March 31, 1991.

(B) As at March 31, 1991 per the 1991 British Columbia Economic and Statistical Review.

(C) Uses crown land at no cost.

(D) Exempt from most property taxes.

(E) Small values not quantified.

(F) Per CRF financial statements